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C O N F I D E N T I A L SECTION 01 OF 02 MANAGUA 002479

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TAGS: [EFIN](#) [EAID](#) [ECON](#) [PREL](#) [PGOV](#) [NU](#)

SUBJECT: GON SLOWLY REACHING OUT TO BUDGET SUPPORT DONORS

REF: A. MANAGUA 2393 (NOTAL)

[B](#). MANAGUA 2255

[C](#). MANAGUA 1933 (NOTAL)

Classified By: Amb. Paul Trivelli for reasons 1.4 b&d.

[1](#)1. (C) Summary: The Budget Support Group (BSG), a group of donor countries providing direct budget support (i.e. cash transfers for development purposes) to Nicaragua, told the Ministry of Finance (MHCP) on October 4 that it could not confirm funds to support the 2008 National Budget without better information as to how these funds would be used (Ref B). As a result, the GON has slowly begun to engage the budget support donors, starting with an October 11 preview of the 2008 Budget by Ministry of Finance (MHCP) staff. BSG members have been concerned that MHCP included unconfirmed donations in the budget for "projection purposes," but MHCP staff claim that the amounts will not be incorporated into the final budget by the National Assembly until confirmed by donors. On October 16, the MHCP tried to pass 10 Millennium Development Goals (social indicators) as the revised indicators for the Performance Assessment Matrix (PAM) which the BSG use to assess the GON's performance. The BSG president returned the list with suggestions for improvement, some of which MHCP included in its second draft of the PAM, delivered October 29. BSG donors still view the GON as a reluctant participant in the budget support process. If this view persists, donors may decide to phase out their direct budget support over the next few years. End Summary.

The GON Finally Reaches Out

[1](#)2. (C) The Budget Support Group (BSG), a group of donors providing direct budget support to Nicaragua, sent a letter to the Ministry of Finance (MHCP) on October 4 stating its unwillingness to confirm donor funds to support the 2008 National Budget without better information as to how these funds would be used (Ref B). As a result, the GON has engaged with the BSG, but has not yet addressed donor issues on the matrix of indicators for 2008 and the required semi-annual meetings. BSG donors are prepared to provide USD 80 million of Nicaragua's USD 1.53 billion 2008 budget. The BSG is composed of the Inter-American Development Bank (new in 2008), the World Bank, the European Union, U.K., Norway, the Netherlands, Germany, Switzerland, and Finland. BSG

observers are the IMF, UNDP, Canada, and the United States.

¶3. (SBU) On October 11, the GON provided a preview of the 2008 National Budget to the BSG (four days before the budget was delivered to the National Assembly), which included a discussion of when and how to include BSG funds. The GON highlighted:

- The fiscal deficit will be close to 1.8% of GDP, the PRGF target;
- Poverty reduction expenditures will be 16.7% of GDP;
- Teachers and health service workers will receive a 12% salary increase;
- The GON will prioritize resources to help the Atlantic Coast region recover from Hurricane Felix, finance municipal elections in November 2008, and transfer capital to the new National Development Bank (Ref A); and,
- MHCP will reduce the number and size of its capital expenditures in 2008 so that spending targets can be met.

¶4. (C) In this meeting, BSG donors focused on how the MHCP accounts for donor funds within the budget. MHCP traditionally creates a draft budget in May, to allow donors to report Nicaragua's needs in time for donor governments to determine financing amounts before the end of the year. When the MHCP submits the budget to the National Assembly in October, it should only include confirmed funds from donors. The MHCP adds any funds confirmed by donors after October via a budget reform law. This year, MHCP decided to include unconfirmed funds from donors for "projection purposes," i.e., to meet the budget deficit targets for the Poverty Reduction and Growth Facility (PRGF), the IMF's low interest lending facility for low-income countries. MHCP assured BSG donors that the Economic Commission at the National Assembly will not include any unconfirmed funds in the budget sent to the floor.

¶5. (SBU) BSG donors also raised concerns regarding inflation and the slow execution of the 2007 capital budget. MHCP staff told donors that the increase in the world price of oil will drive Nicaragua's inflation, minimizing the effect of GON policy in other areas, such as reducing banks' reserve requirements by 3%. Consistent with the FSLN's criticism of donor assistance projects, MHCP staff blamed the slow execution of the 2007 capital budget on "administrative problems and high execution costs." (Comment: In reality, slow execution is the result of the presidency meddling in ministry affairs and the lack of technically experienced staff after the wholesale turnover in government personnel orchestrated by the Ortega administration (Ref C). End Comment.)

The GON Tries for an Easy Score

¶6. (C) On October 16, the MHCP sent the BSG a proposed Performance Assessment Matrix (PAM) which contained 10 indicators, copied from the IMF Poverty Reduction Growth Facility (PRGF) and based on the United Nations' Millennium Development Goals, focused primarily on social issues. The BSG's yearly review of GON performance is based upon this one coordinated matrix of indicators organized under the broad topics of macroeconomy, public finance, social issues, governance, and productivity. In comparison with the 54 indicators in the 2006 PAM, these ten indicators lacked the quality and breadth essential for an effective PAM (Ref B). BSG President Joseph Owen recommended that the GON broaden and improve the quality of the list.

¶7. (C) On October 30, the GON forwarded a new matrix with 24 indicators covering macroeconomic, social, and production issues and eliminating good governance and public finance. The BSG technical committees will comment on these indicators, and propose additions and modifications at the semi-annual review meeting, which must take place before December 31. This meeting was finally scheduled for November 19, on two working-days' notice.

Background: IMF role in the BSG process

18. (C) While having a PRGF is not a requirement for BSG donors, the goal of achieving and maintaining macroeconomic stability is. Most BSG donors believe that an active PRGF encourages the government to pursue policies that support a stable macroeconomic environment. A good PRGF and a quality PAM help donors to justify their programs at home. As an observer to the BSG, the IMF ResRep was unaware of the BSG's growing frustration with the GON until a few days before the IMF Board meeting in October where the PRGF was approved (Ref B).

Comment

19. (C) Despite its recent effort to engage the BSG, the GON continues to frustrate donors who feel the government is a reluctant participant in the budget support process. Every request for a meeting must be repeated, and meetings are often delayed or postponed. The BSG's work calendar is continually slipping, increasing frustration among local donor agencies and their capitals. If GON truculence continues, donors may reduce their direct budget support over the next few years, as they conclude that they cannot justify the funds. Should donors pull out of multi-year commitments, the GON could lose the majority of its budget support by 2010.

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